RECORD KEEPING AND SOME BASIC CONCEPTS

Learning Objective

The evolution of accounting stated in the previous lecture continues with a slight emphasis on how actual record keeping started? In addition, some basic concepts like capital, profit, and budget are also introduced.

Different Types of Business Entities

- **Commercial Organizations (Profit Oriented)**
  - Sole proprietor
  - Partnership
  - Limited companies

- **Non-Commercial Organizations (Non-Profit Oriented)**
  - NGO’s (Non-government Organizations)
  - Trusts
  - Societies

The Basic Concept of Record Keeping

We can maintain a diary of transactions and note the daily transactions like sale, purchase etc. in it.

Problems Faced in Maintaining Diary of Transactions

- How will we come to know the income and expenses from various sources?
- We only have a sheet / page on which daily transactions are listed.
- We do not know which product is selling better and which is not.

Diary of Transactions

<table>
<thead>
<tr>
<th>Transactions of Jan 20--</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sold 5 nos. of Item A</td>
<td>1,000</td>
</tr>
<tr>
<td>Purchased 10 nos. of Item B</td>
<td>(15,000)</td>
</tr>
<tr>
<td>Sold 1 no. of Item C</td>
<td>2,000</td>
</tr>
<tr>
<td>Electricity bill paid</td>
<td>(1,500)</td>
</tr>
<tr>
<td>Sold 1 no. of Item A</td>
<td>500</td>
</tr>
<tr>
<td>Sold 2 nos. of Item B</td>
<td>4,000</td>
</tr>
<tr>
<td>Sold 5 nos. of Item A</td>
<td>1,000</td>
</tr>
</tbody>
</table>
Available Alternate

One can go through all the transactions at the end of the month and note different types of transactions on different pages. So that every page gives complete detail for a different type of transaction like sales of different products and expenses of different types. Now try to go through these transactions and separate transactions of different types.

But what if the number of transactions is large?

Is it really possible to go through hundreds or thousands of transactions at the month end and analyse them to obtain required results.

Cash and Credit Transactions

Sales and purchase are not always for cash. Some times the payment / receipt is delayed to a future date (Sale/purchase for “UDHAR”). The diary that we have discussed above, records cash transactions only. The “UDHAR” (credit) transactions may be noted in separate diary. Now we have two diaries one for cash and one for credit. We need to know total sales and purchases (both cash and credit) and other information like the amount that is payable and receivable.

How will we get our required results now?

Do we need another diary to combine information from both these diaries? But when we receive or pay cash for the credit transactions will we again record the transactions on the day,

When cash is received or paid? If so, where to record?

So the problems keep on increasing with the size or volume of business. But one thing is becoming certain and that is that an accurate reflection of business transacted can only be obtained if both cash and credit transactions are recorded in such a manner that there is no duplication and yet the transactions are completely recorded. This is possible only under Commercial Accounting.

Commercial Accounting

Commercial Accounting is done through a system that is known as Double entry book keeping.

Single Entry and Double Entry Accounting

- Single entry accounting/Cash accounting.
This system records only cash movement of transactions and that too up to the extent of recording one aspect of the transactions. This means that only receipt or payment of cash is recorded and no separate record is maintained (about the source of receipt and payment) as to from whom the cash was received or to whom it was paid.

- **Double entry book keeping/Commercial accounting.**

Double entry or commercial accounting system records both aspects of transaction i.e. receipt or payment and source of receipt or payment. It also records credit transactions i.e. recording of Electricity Bill or accruals of Salary payment etc.

This concept will be explained in detail in the next lectures but for the time being it should be noted that in cash accounting date of receipt / payment of actual cash is important while in commercial accounting the date on which the expense is caused (whether paid or not) as well as the spreading of the cost of certain items over their useful life becomes important.

**Capital**

No business can run without money or resources being invested therein.

Whatever money or resources from ones’ own pocket are put in a business is referred to as **CAPITAL.** Capital is the investment of the Owner in the business. This capital or investment must earn a return or profit on its use even if it is coming out of ones’ pocket. This return is also known as **PROFIT.** So no capital should be without a profit or a return. Also, no Capital even if coming from the business owner can be without cost. Why? Because if the same sum that was used in a business was put in the bank or used to buy Defence Savings or National Savings Certificates, a certain amount of profit would have been earned. By putting this money in business, a return must be expected.

**Money Value of Time**

Another important concept to remember in all businesses is that of **MONEY VALUE OF TIME.**

Time spend by the owner also has value; he should be remunerated for it. (The time of the proprietor or business persons spent on the business is also a business cost and must be paid for by the business in addition to the profit). Why because, if the business person had employed somebody else in his place, the person would be paid a salary. Therefore, a business person’s **time and money** both have costs attached to them. Nothing is free nor should be expected to be free of cost.

**Goodwill**

This is simply the value attached to the good reputation earned through good and clean conduct of business over a number of years. This good reputation also has a value and becomes part of investment in business.
Is Cash in Hand our Profit?

Not unless we have deducted from cash sales it is the total amount of expenses that are accrued or are on credit and added to it to the sales made on credit for which cash is to be received at a later date. The simple equation for calculation of profit would thus be:

\[
\text{Cash Sale - Cash Payment} + (\text{Credit Sale - Credit Expense})
\]

Also remember that certain items have a long life and will be used during that time to earn more money for business. The cost of such items will as be spread over their life and also accounted for accordingly in the above equation.

Budget

Budgeting is another important aspect of business planning. The budget is made to ensure that there is at least a balance between Income earned and the expenses incurred on earning this income in the first instance, and to provide a reasonable return on the capital used in the business. However, if there is a shortfall between of Income as against expense, it means that more is being spent and less earned. Decisions will be required to bring the situation to balance or if it cannot be so then to arrange for loans or more capital to ensure business continues. But business cannot be run on loans and these must be repaid.

Budget Is an Organization’s Plan of a Future Period Expressed in Money Terms.